



New Designs: Licenses May Be Evidence of the Nonobviousness of an Invention

BY JOHN T. MCNEELIS

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A license agreement frequently transfers some rights in an invention from a patent owner to a licensee. Such a license agreement can be used during litigation or during the patent application process as evidence of nonobviousness of the invention. That is, a license may help the patent owner prove that a patent is valid and may even help the licensor obtain a patent that is directed toward the licensed technology.

Whether the claimed invention is obvious in view of the prior art is a difficult question relating to the patentability of an invention. This issue of obviousness frequently arises during patent prosecution, reexamination proceedings, and litigation. The Supreme Court set forth four factors that the courts must consider when determining whether a claimed invention is invalid because it is obvious. The court must identify: (1) the scope and content of the prior art, (2) differences between the prior art and the claims at issue, (3) the level of ordinary skill in the pertinent art, and (4) "objective" or "secondary" considerations, such as whether there was a long-felt need for the claimed invention, the failure of others, or whether the claimed invention has enjoyed commercial success. *Graham v. John Deere Co.*, 383 U.S. 1, 17-18 (1966).

The courts use secondary considerations to, inter alia, focus attention on the economic and motivational issues rather than on technical issues. The economic and motivation issues are "more susceptible of judicial treatment than are highly technical facts often present in patent litigation." *Id.* at 36. The Federal Circuit has found that "evidence of secondary considerations may often be the most probative and cogent evidence in the record." *Stratoflex Inc. v. Aeroquip Corp.*, 713 F.2d 1530, 38 (Fed. Cir. 1983), see also *In re Mayne*, 104 F.3d 1339 (Fed. Cir. 1997). Two examples of secondary considerations are the commercial success of the claimed invention and the commercial acquiescence by market competitors. Licenses can be used as evidence of either of these secondary considerations.

The commercial success of a product embodying a claimed invention is often used as evidence of nonobviousness. The courts suggest that evidence of commercial success is relevant to the question of obviousness because competitors would have been economically motivated to make the invention before the inventor if the invention had been obvious. *Minnesota Mining & Manufacturing Co. v. Research Medical Inc.*, 679 F. Supp. 1037, 1054 (D. Utah 1988). The courts proffer that if the commercial success is based upon the capturing of a large market share or upon the licensing of the invention to many competitors, such actions tend to support the finding that the claimed invention is superior to existing products and is therefore a nonobvious advance over the prior art. *Tennant Co. v. Hako Minuteman, Inc.*, 22 USPQ2d 1161, 1177 (N.D. Ill. 1991). Evidence of commercial success includes a showing of growth in market share, a decrease in market share after other companies begin infringing, and licensing to other companies.

The commercial acquiescence of a claimed invention is also used as evidence of nonobviousness under the theory that a license is generally a statement against the licensee's interest. That is, a licensee does not generally act in a manner contrary to his economic self interest unless convinced of the validity of the patent or of the nonobviousness of the claimed invention in a pending patent application.

Of course, commercial success or a successful licensing campaign can occur for a variety of reasons that are unrelated to the validity of a patent. Therefore, the courts have required not only evidence of commercial success or acquiescence but also a showing of a nexus between the evidence and the claimed invention. The term "nexus" refers to a legally and factually sufficient connection between the proven success and the claimed invention. *In re Paulsen*, 30 F.3d 1475, 1482 (Fed. Cir. 1994). The stronger this connection, the stronger the evidentiary value of the commercial success. *In re GPAC Inc.*, 57 F.3d 1573, 1580 (Fed.

Cir. 1995). A nexus is proven when the commercial success or commercial acquiescence is shown to have been due to the nature of the claimed invention, as opposed to other economic and commercial factors unrelated to the technical quality of the claimed invention. *Cable Electric Products, Inc. v. Genmark, Inc.*, 770 F.2d 1015, 1027 (Fed. Cir. 1985). If a license covers many patents, only one of which is directed toward the claimed invention, the patent owner must show that the license arose out of a "recognition and acceptance" of the relevant patent. *Stratoflex* at 1539.

When licenses are used as evidence of commercial success or commercial acquiescence, the evidentiary value given to the licenses depends upon the contents of the licenses and the nexus between the licenses and the claimed invention. The factors that are considered when determining the evidentiary value of the licenses include the royalty rate when compared to the cost of litigation, pre-license investigation by the licensees, the market position of the licensees, the market share of the licensees, and the nexus between the license and the claimed invention.

When the royalty rate paid by a licensee is large when compared to the cost of litigation, the license will be persuasive evidence that the licensee believed the patent was valid. *B&H Manufacturing Inc. v. Foster-Forbes Glass Co.*, 26 USPQ2d 1066, 1070 (N.D. Ind. 1993). Licensees who perform a significant investigation into the validity and infringement of the patents covered by the license strengthen the evidentiary value of the license for the purpose of later proving nonobviousness. *RCA Corp. v. Data General Corp.*, 701 F. Supp 456, 471 (D.Del. 1988), *aff'd*, 887 F.2d 1056 (Fed. Cir. 1989). The market position of the licensees is a factor in determining the strength of the evidence under the theory that industry leaders are less likely to obtain a license unless they believe the patent is valid. In *B&H Manufacturing*, two of the licensees of the patent were "the most powerful bottling companies in the country" which led the court to believe that "they would not have bowed to pressure to take a license without first reaching the conclusion that ultimately litigation would prove futile." *B&H Manufacturing* at 1070. A patent on a color television picture tube was similarly upheld based in part on the fact that "the leader in color television development" chose to license the patent. *Columbia Broadcasting Sys. v. Sylvania Elec. Prods., Inc.*, 415 F.2d 719, 728 (1st Cir. 1969), *cert denied*, 396 U.S. 1061 (1970). The combined market share of the licensees is also relevant. The Supreme Court held that when the makers of two-thirds of the print paper of the country are licensees of the patent

holder this constitutes "weighty evidence" of the validity of the patent. *Eibel Process Co. v. Minnesota & Ontario Paper Co.*, 261 U.S. 45 (1923).

Courts have found that licenses do not provide enough evidence of nonobviousness when the royalty rate is low when compared to the cost of litigation, the percentage of the relevant market controlled by the licensees is low, when the license represents a mutually beneficial arrangement, or when the nexus between the license and the claimed invention is not shown.

The courts are in agreement that if the royalty rate of a license is low in comparison to the cost of a litigation defense, the licensee's motivation for obtaining a license is more likely to avoid litigation rather than a belief that the patent was valid. This is a particularly strong motivation when the licensee is a small business having limited resources. The Supreme Court notes that when a license has a low royalty rate the "purchase of peace" may be the motivation for a small business and therefore the license is of limited value as evidence of patent validity. *John E. Thropp's Sons Co. v. Seiberling*, 264 U.S. 320, 329-30 (1924). Courts also look to the market share and size of the licensees. In *Phillips Elec. & Pharmaceutical Indus. Corp. v. Thermal & Elec. Indus., Inc.*, 450 F.2d 1164 (3d Cir. 1971), eleven manufactures of glass-to-metal seals obtained licenses under the patent. The court noted that the none of the major companies in the market obtained a license, the total market share of the eleven licensees was low and that it was possible that the licensees found acquiescence less burdensome and costly than the expense and problems of litigation. The courts indicate that another motivation for entering a license agreement is that a license may be mutually beneficial to both the licensee and the licensor. When a license is mutually beneficial the evidentiary value of the license as a secondary consideration is limited. *EWP Corp. v. Reliance Universal Inc.*, 755 F.2d 898, 907-08, (Fed. Cir.), *cert denied*, 474 U.S. 843 (1985). For example, an exclusive license may be mutually beneficial since the licensee will have exclusive rights to make, use, offer to sell, and sell the invention.

When attempting to overcome an obviousness argument the patent practitioner should identify licenses and other evidence that demonstrates the commercial success of a claimed invention and then clearly explain the nexus between the evidence and the claimed invention in order to maximize its evidentiary value.